VZCZCXRO3364
RR RUEHBZ RUEHGI RUEHTRO
DE RUEHFR #1872/01 2841459
ZNR UUUUU ZZH
R 101459Z OCT 08
FM AMEMBASSY PARIS
TO RUEHC/SECSTATE WASHDC 4479
INFO RUEATRS/DEPARTMENT OF TREASURY WASHDC
RUEKJCS/SECDEF WASHINGTON DC
RUEHRL/AMEMBASSY BERLIN 6854
RUEHSW/AMEMBASSY BERN 2138
RUEHBS/AMEMBASSY BRUSSELS 6810
RUEHCP/AMEMBASSY COPENHAGEN 1598
RUEHLO/AMEMBASSY LONDON 6993
RUEHMD/AMEMBASSY MADRID 2864
RUEHMO/AMEMBASSY MOSCOW 6189
RUEHNY/AMEMBASSY OSLO 1644
RUEHRO/AMEMBASSY ROME 8931
RUEHSM/AMEMBASSY STOCKHOLM 1664
RUEHTC/AMEMBASSY THE HAGUE 3019
RUEHKO/AMEMBASSY TOKYO 2833
RUEHBS/USEU BRUSSELS 2392
RUEHLU/AMEMBASSY LUANDA 0987
RUEHGI/AMEMBASSY BANGUI 0264
RUEHRY/AMEMBASSY CONAKRY 0087
RUEHBZ/AMEMBASSY BRAZZAVILLE 0171
RUEHGB/AMEMBASSY BAGHDAD 0128
RUEHAM/AMEMBASSY AMMAN 1217
RUEHMV/AMEMBASSY MONROVIA 7385
RUEHTH/AMEMBASSY ATHENS 0786
RUEHKI/AMEMBASSY KINSHASA 1672
RUEHAB/AMEMBASSY ABIDJAN 1267
RUEHLC/AMEMBASSY LIBREVILLE 1409
RUEHPU/AMEMBASSY PORT AU PRINCE 0878
RUEHPC/AMEMBASSY LOME 1136
RUEHBU/AMEMBASSY BUENOS AIRES 1577
RUEHKH/AMEMBASSY KHARTOUM 0331
RUEHWR/AMEMBASSY WARSAW 0869
RUEHBR/AMEMBASSY BRASILIA 2070
RUEHCH/AMEMBASSY CHISINAU 0425
RUEHJB/AMEMBASSY BUJUMBURA 0115
RUEHTRO/AMEMBASSY TRIPOLI 0173
RUEHBJ/AMEMBASSY BEIJING 1787
RUEHUL/AMEMBASSY SEOUL 1568
RUEHAK/AMEMBASSY ANKARA 0969
RUEHTV/AMEMBASSY TEL AVIV 0015
RUEHSA/AMEMBASSY PRETORIA 1584
RUEHKU/AMEMBASSY KUWAIT 0247
RUEHAD/AMEMBASSY ABU DHABI 0275
RUEHPL/AMEMBASSY PORT LOUIS 0989
RUEHPS/AMEMBASSY PRISTINA
RUEHIL/AMEMBASSY ISLAMABAD 0776
RUEHDJ/AMEMBASSY DJIBOUTI 0903
RUEHBH/AMEMBASSY NASSAU 0087
RUEHUB/USINT HAVANA 0090

UNCLAS SECTION 01 OF 16 PARIS 001872

SENSITIVE
SIPDIS

STATE FOR EEB/IFD/OMA
TREASURY FOR DO/IDD AND OUSED/IMF
SECDEF FOR USDP/DSCA
PASS EXIM FOR CLAIMS - MPAREDES
PASS USDA FOR CCC -- ALEUNG/WWILLER/JDOSTER PASS USAID FOR CLAIMS --
WFULLER
PASS DOD FOR DSCS -- PBERG

E.O. 12958: N/A
TAGS: EFIN ECON EAID XM XA XH XB XF FR
SUBJECT: PARIS CLUB - SEPTEMBER 2008 TOUR D'HORIZON AND DISCUSSIONS
ON METHODOLOGICAL ISSUES

¶1. (SBU) Summary: At the Paris Club's September 17 session, Club
Chairman Musca briefed creditors on recent contacts with the
Government of Argentina (GOA), which revealed that Argentina intends

to clear arrears excluding late interest and resume debt service on future installments. Creditors instructed Musca to urge the GOA to follow through on Christina Fernandez de Kirchner's September 2 announcement that Argentina would pay arrears and late interest in full, in addition to resuming debt service. Several creditors indicated a willingness to consider concessions on late interest similar to what the Club provided on an exceptional basis to Angola in 2007; however, others, including the U.S., expressed opposition to an "Angola-style" solution. All creditors other than the U.S. voiced support for initiating technical discussions with Cuba that could lead to a debt restructuring agreement outside of the Paris Club framework. The IMF reported on discussions with the Democratic Republic of Congo (DRC) aimed at revising the $9 billion infrastructure and mining agreement with China, noting that the Fund's concerns about debt sustainability would need to be addressed before a new IMF program and full debt cancellation could proceed.

¶2. (SBU) Creditors reluctantly agreed to enter into force the second and third phases of Grenada's 2006 debt rescheduling, despite the country's unsatisfactory economic reform performance. Creditors finalized the Paris Club Secretariat's submission on debt-related aspects of the Financing for Development review conference in Doha. There was no consensus to modify the Paris Club's long-standing policy to exclude all leases from debt treatments, although the Netherlands requested further clarifications. Additional countries and methodological topics discussed included Burundi, Georgia,

Pakistan, Seychelles, the Paris Club's work program on methodological issues, a comprehensive data call on Paris Club claims owed by all debtor countries, policy on the entry-into-force of phases in debt restructuring agreements, access to detailed debt data in advance of negotiations, and the IMF/World Bank progress report on implementation of the Heavily Indebted Poor Countries (HIPC) and Multilateral Debt Relief Initiatives (MDRI). End Summary.

¶3. (U) For additional information on a specific country or issue, please contact Nicholle Manz or David Freudenwald in EEB/IFD/OMA.

Argentina

¶4. (SBU) Paris Club Chairman Musca briefed creditors on his recent talks with Argentine Finance Secretary Lorenzino. Musca sought creditors' agreement on the Club's proposed response to Lorenzino, procedures for dealing with the Argentine government, and communications. Contrary to President Cristina Fernandez de Kirchner's announcement that Argentina would pay off its Paris Club debt in full, Argentina intends to clear arrears excluding late interest and resume debt service on maturities falling due. Creditors agreed that the Paris Club should demand full payment of arrears and late interest (in addition to a resumption of current debt service). Payment in full is the simplest and cleanest solution.

¶5. (SBU) Most creditors expressed a willingness to consider some restructuring if necessary to close a deal. The U.S. and Japan voiced the strongest opposition to accepting less than full repayment, although the U.S. explained that it would not block others from offering concessions provided all creditors were repaid on the same schedule. The pressure is now on Argentina to meet expectations it had created for itself. Club cohesion, including with regard to export credit agencies'(ECAs) policies toward Argentina, is also important. Creditors agreed with Musca's suggestion that all data reconciliation and communication with the Argentine authorities be handled by the Secretariat.

¶6. (SBU) Anticipating media queries about the September 17 meeting, the Paris Club issued a brief press release hailing the GOA's announced intention to pay in full its debt to the Paris Club as "a

very significant step towards the normalization of Argentina's relationship with all its external creditors."

¶7. (SBU) The Secretariat provided preliminary analysis of debt data discrepancies. According to Paris Club figures, Argentina's arrears (excluding late interest) amounted to $5.7 billion as of March 2008. According to Argentine figures, the number is $4.9 billion. Of the $812 million difference, the Secretariat attributed $647 million to loans which were previously reconciled with Argentina in 2003 but which the government apparently overlooked in its most recent submission.

Burundi

¶8. (U) The IMF reported that Burundi could qualify in early 2009 for completion point and full HIPC debt cancellation when the IMF executive board considers the first review of Burundi's new Poverty Reduction and Growth Facility (PRGF) program. An IMF mission is scheduled to visit Burundi to conduct the review in late October or early November 2008. Creditors agreed with the Secretariat's proposal to resume interim HIPC debt relief by retroactively extending the consolidation period of the previous Paris Club agreement through mid-2009. The other option would have been to negotiate a new agreement that folded in arrears, as in the case of Congo-Brazzaville (see para 9). The Secretariat argued that, in contrast to Congo-Brazzaville, Burundi had fewer Paris Club creditors and was rapidly approaching completion point; hence, the option to retroactively extend the consolidation period made more sense. (The U.S. is not a creditor.)

Republic of Congo (Brazzaville)

¶9. (SBU) The IMF said staff had agreed ad referendum with the authorities on a new PRGF. Assuming technical discussions conclude successfully in the following weeks, the IMF will ask the Paris Club for financing assurances at the October meeting. Negotiations with the Paris Club are expected in November. Creditors agreed to resume interim HIPC debt relief by negotiating a new agreement with

Congo-Brazzaville on Cologne terms, which will treat arrears that accumulated since 2006, when Congo's previous IMF program went off-track. The Secretariat argued that negotiating a new agreement was preferable to retroactively extending the previous consolidation period given the long off-track period and the fact that recrediting payments already received posed legal difficulties for some creditors. (When retroactively extending a previous consolidation period, creditors are required to recredit or refund payments received in excess of what would have been due had the previous Paris Club agreement been in force.) The UK asked the IMF if it had any information about three new loan agreements that Congo-Brazzaville concluded with China. The IMF said it did not, but noted that the new PRGF would prohibit all non-concessional borrowing. The Secretariat said the authorities' July 25 response to the Paris Club's letter of April 1 failed to provide any details on agreements reached with litigating creditors.

Cuba

¶10. (SBU) The Cuban central bank approached the Secretariat seeking a technical meeting with a "group of creditors," with the possibility that such a meeting could lead to negotiations. (Note: In 2000 and 2001, a group of creditors, excluding the U.S., held inconclusive discussions with Cuba on a possible multilateral debt treatment. End Note.) Cuba sought a letter from the Secretariat,

on behalf of the group of creditors, regarding a technical meeting. Spain, Italy, Denmark, Belgium, Canada, Finland, UK, Netherlands,

Sweden, Russia, and Austria welcomed the opportunity to restart the dialogue that stalled in 2001. Australia asked how such a "group of creditors" would work. Given that Cuba is not a member of the IMF, what would substitute for the IMF's role? The Secretariat said it would review how the discussions proceeded in 2001 and mentioned use of Economist Intelligence Unit data. Spain suggested an informal approach, with the Cuban side initiating correspondence. Canada noted that it was having difficulty getting Cuba to pay short-term debt. The Netherlands supported resuming contacts, but noted that Cuba had not paid for two years. Russia was strongly interested in seeing the Cubans and strongly appreciated the Secretariat's efforts. The U.S. was the only creditor to express opposition, pointing out that any agreement to provide treatment to an uncooperative and non-reforming Cuba would stand in stark contrast to the economic reform performance requirements the Club imposes on other poor countries. The Secretariat said that since Cuba is not an IMF member, a formal Paris Club agreement would not be possible. Coeure noted creditors' strong interest but also a need to weigh the consequences, including how providing debt relief to Cuba in the absence of an IMF program could impact the Club's position vis-a-vis Argentina. As a first step, the Secretariat will circulate an aide-memoire reminding creditors of discussions with Cuba in 2000 and 2001.

Djibouti

¶11. (U) The IMF thanked creditors for providing financing

assurances by e-mail prior to the IMF executive board's September 17 discussion of Djibouti's new PRGF. Approval of the program paves the way for Djibouti to come to the Paris Club later this year for a debt treatment under the Evian approach. The Secretariat summarized its working paper, which recommends that the Paris Club provide Djibouti an initial rescheduling of arrears and future installments, together with a commitment by creditors to provide further relief at a future date if necessary to restore debt sustainability.

Democratic Republic of Congo (DRC)

¶12. (SBU) The IMF outlined its concerns with the DRC's $9 billion mining and infrastructure agreement with China. (These concerns are described in detail in an August 29 letter from the IMF and World Bank to DRC Prime Minister Gizenga.) The IMF said its concerns would need to be addressed before staff could move forward with a new PRGF program for the DRC. The primary concerns include the sheer size of the deal, direct/indirect sovereign guarantees, earmarking of revenues to repay the Chinese, and the non-concessional nature of the financing. Under the latest debt sustainability analysis, the current deal would render the DRC's debt unsustainable even after full HIPC debt forgiveness. The IMF and DRC authorities are discussing options to deal with these issues. The World Bank noted that new non-concessional borrowing by the DRC would trigger a 20 percent reduction in International Development Association grants. Japan summarized the G-7 deputy finance ministers' August 27 letter to the IMF, which indicated that the G-7 "may have great difficulty

providing financing assurances for a future IMF program" if the sovereign guarantees remained in place. The Secretariat stressed that the letter was not meant to suggest that the DRC could not borrow from China, but rather that any new borrowing must be consistent with HIPC guidelines. Italy asked whether the IMF had raised these matters with the Chinese; the IMF said it should not

negotiate with a creditor on behalf of a debtor. Nevertheless, the Fund representative acknowledged the PRC is aware of the issues but unwilling to engage on the DRC. The UK praised the IMF for taking a strong position and suggested that the Paris Club consider sending a letter to the DRC authorities, depending on the outcome of current discussions between the authorities and IMF staff. The Secretariat said the Paris Club could revisit the UK's suggestion next month. Belgium, the only non-G-7 member to comment, noted that it would not be easy for the DRC to renegotiate a deal that had already been struck.

Georgia

¶13. (SBU) The IMF described the pressures that the Georgian economy is experiencing and said a $750 million Stand-by Arrangement (SBA) had just been approved. Russia said approval of the SBA by the IMF's executive board "deviated from standard procedure," reflecting high-level political interference. Russia further commented that under Georgia's 2001 and 2004 Paris Club reschedulings, the Georgian government committed to implement social and economic reforms, including spending to reduce poverty, but instead ramped up military

spending. Therefore, if Georgia requested a new debt treatment, the Paris Club would need to examine the request carefully. The Secretariat responded that it did not anticipate that Georgia would seek further debt relief from the Paris Club.

Grenada

¶14. (SBU) Creditors agreed to enter into force the second and third phases of Grenada's May 2006 rescheduling, covering installments falling due in 2007 and 2008, despite the fact that Grenada's performance on its IMF program in 2007 was unsatisfactory. Russia said it would not block consensus, although its preference was not to enter into force the second phase because doing so would weaken the conditionality principle. The U.S. expressed strong reservations about not enforcing the Paris Club's conditionality principle but agreed to go along with Secretariat's recommendation in this case this time on an exceptional basis. The IMF acknowledged that it had not contemplated the possibility that the Paris Club might not enter into force the second phase, even though all Paris Club agreements clearly stipulate that debt relief is tied to the debtor country's implementation of economic reforms. The IMF said non-entry into force of the second phase would have placed Grenada's PRGF program under stress and forced staff to reconsider the program's financing.

Pakistan

¶15. (SBU) The IMF reported that macroeconomic conditions had deteriorated markedly due to adverse political and security developments, oil and food price shocks, and policy inaction during and after the political transition. Pakistan faces large financing gaps, which it is trying to fill through accelerated privatizations and bilateral support. The GOP had requested an oil facility from Saudi Arabia, but terms and timing are uncertain. Even if the GOP were to obtain $5 billion per year from the Saudis, more financing would be needed for this year. It is unclear at this time whether the government will seek an IMF program. Asked to estimate the financing gap, the IMF rep declined, saying financing commitments are not clear. The World Bank added that the GOP needs to take policy actions and present a serious reform framework to donors; the Bank can then adapt its lending strategy, and donors will need to step up. Russia complained that a $163 million payment from Pakistan had been blocked by the Pakistani authorities. Russia said

it planned to raise the issue in the IMF executive board.

Seychelles

¶16. (U) The IMF said the Seychelles was suffering from food and oil price shocks, a foreign exchange shortage, inflation at 34 percent, and large financing gaps. In July, the government defaulted on a 55 million euro amortizing note, prompting holders of the notes to accelerate payments and leading S&P to downgrade its credit rating

for the Seychelles. The authorities have hired financial and legal advisors and held an initial meeting with a creditor committee in August. Meanwhile, the authorities have had constructive discussions with IMF staff about a possible program. A request for an SBA could come to the IMF executive board in November, in which case the IMF would request financing assurances in early November. Seychelles cleared its arrears to the World Bank last year. (The U.S. is not a creditor.)

Methodological Discussion:
Work Program of Methodological Issues

¶17. (U) Creditors approved the proposed work program of methodological issues for the remainder of 2008 and the first quarter of 2009, including the following topics:

-- A Paris Club submission to the Doha Conference on Financing for Development;

-- Outreach to non-Paris Club creditors and update on contacts with private creditors regarding litigation against HIPCs;

-- A global, aggregated data call of Paris Club claims on all debtor countries;

-- Seniority rules and their impact on Paris Club debt treatments;

-- Links between Paris Club debt treatments and the IMF;

-- Paris Club treatments for fragile states (in the absence of an IMF program with conditionality);

-- Sustainable lending and ODA loan policies;

-- Illegitimate debt (for internal Paris Club discussion only);

-- Debt buybacks and comparable treatment; and

-- Financial leases (discussion and review of the September Working Paper; there is no consensus to change Paris Club policy - see para 20.).

¶18. (SBU) Germany requested to add the topic of illegitimate debt to the work program; Norway agreed. Italy, Netherlands, the UK, and the U.S. all questioned why the Paris Club should spend any time on a concept that many Paris Club member governments do not recognize. Germany argued that it would be helpful to exchange views on how to respond to NGOs. In the end, creditors agreed that the discussion would be strictly internal and non-binding.

Methodological Discussion:
Paris Club Input to Doha Conference

¶19. (SBU) Creditors agreed to submit a Paris Club working paper to

the Financing for Development review conference that will take place in Doha from November 29 to December 2. The working paper provides the Paris Club's assessment of the implementation of the Monterrey Consensus as it relates to external debt, and articulates policy recommendations on debt issues. The Secretariat drafted the paper with input from Paris Club members and is broadly consistent with USG views. Spain and Germany requested mention of the Sovereign Debt Restructuring Mechanism (SDRM) proposal, which they had supported in 2002; given lack of Club consensus, however, the Secretariat devised a neutral reference to past discussion of the concept.

Methodological Discussion: Leasing

¶20. (U) Based on the results of the recent questionnaire, the Secretariat recommended that the Paris Club retain its policy of excluding all lease arrangements from Paris Club treatments. Germany, Norway, and the U.S. voiced support for this recommendation. The Netherlands, however, said it needed more information on financial leases -- in particular, their volume and potential impact on a debtor country's capacity to pay -- before it could give its consent. The Secretariat agreed to do more analysis and added the topic to the work program of methodological issues. The Netherlands asked whether a creditor could voluntarily include a lease arrangement, or whether all lease arrangements had to be excluded. The Secretariat said this particular point was not addressed in the questionnaire and therefore was open to discussion.

Italy asked to include this item in the Paris Club's Work Program (see para 17).

Methodological Discussion:
Data Call on All Paris Club Claims

¶21. (U) Creditors agreed to participate in a global data call that will aggregate the Paris Club's claims (both non-ODA and ODA) for each debtor country. The results will be made public and updated periodically. The Secretariat will share the disaggregated data on a confidential basis with Paris Club members and the IMF. The Secretariat will prepare a chart on how creditors currently treat such information.

Methodological Discussion:
Entry-into-force of Phases
in Paris Club Agreements

¶22. (U) The Secretariat proposed measures to make the Paris Club's process of entering into force phases of debt relief more transparent and predictable. The aim is to avoid a recurrence of what transpired with Grenada, where the IMF was caught off guard when the Paris Club seriously contemplated not entering into force the second phase of Grenada's 2006 agreement. The U.S. asked the Secretariat to clarify precisely which IMF review would trigger

entry into force of a given phase. The Secretariat's response led to more questions, and the discussion ultimately bogged down. The Secretariat promised to revise its working paper to try to clarify some of the issues raised.

Methodological Discussion:
Sending Detailed Debt Tables
to All Creditors

¶23. (U) In response to Germany's request, the Secretariat agreed to share detailed data call results with all Paris Club creditors ahead of all future negotiations. (In recent years, the Secretariat has distributed a summary of the results, rather than a loan-by-loan breakdown for each creditor.) The Secretariat will share the earliest version of the data call available and alert creditors if the numbers change significantly before the negotiations.

Methodological Discussion:
HIPC and MDRI Progress Report

¶24. (U) The IMF summarized its 2008 progress report on the implementation of HIPC and MDRI. Among the report's key findings:

-- Significant debt relief has been delivered in a flexible manner that accommodates country circumstances while preserving core

principles. The positive results achieved include reduced debt burdens, increased poverty reduction-related spending, and improvements in broader macro-economic aggregates.

-- Debt relief constitutes only a small fraction of net aid inflows to HIPCs. Additional aid flows are urgently needed to address HIPCs' development needs.

-- About 40 percent of non-Paris Club bilateral creditors participate in HIPC.

-- Commercial creditors' participation in HIPC has increased, although litigation remains an issue.

-- Reaching completion point is a challenge for the remaining HIPCs.

-- Debt sustainability remains a challenge even after debt relief. Of the 23 post-completion point HIPCs, four are judged to have a high risk of debt distress.

-- Debtors must maintain prudent borrowing policies, and creditors must promote sustainable lending policies and capacity building.

STAPLETON